Legislative Audit Division

State of Montana

Report to the Legislature

October 2006

Financial-Compliance Audit

For the Two Fiscal Years Ended June 30, 2006

Department of Corrections

This report contains twelve recommendations to the Department of Corrections. Issues in the report include:

- **Control structure**
- **Financial accountability**
- **Contract administration and monitoring**
- **Contractor payments**
- **Compliance with state laws**

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LEGISLATIVE AUDIT DIVISION

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October 2006

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report for the Department of Corrections for the two fiscal years ended June 30, 2006. This report contains twelve recommendations related to the department's control structure, various aspects of financial accountability, monitoring and administration of contracts, contractor payments, and compliance with state laws. The department's written response to audit recommendations is included at the end of the audit report.

We thank the director and his staff for their assistance and cooperation throughout the audit.

Respectfully submitted,

/s/ Scott A. Seacat

Scott A. Seacat
Legislative Auditor

Legislative Audit Division

Financial-Compliance Audit
For the Two Fiscal Years Ended June 30, 2006

Department of Corrections

Members of the audit staff involved in this audit were Laurie Barrett, Paul O'Loughlin, Vickie Rauser, Melissa Soldano, and Lena Tamcke.

Table of Contents

Table of Contents

Director's Office	Mike Ferriter, Director
Health, Planning, & Information Services Division	Gary Hamel, Division Administrator
Administrative & Financial Services Division	Rhonda Schaffer, Division Administrator
Community Corrections	Pam Bunke, Division Administrator
Youth Corrections	Steve Gibson, Division Administrator
Secure Custody Facilities	Mike Mahoney, Warden, Montana State Prison Jo Acton, Warden, Montana Women's Prison
Human Resources	Steve Barry, Division Administrator
Montana Correctional Enterprises	Gayle Lambert, Division Administrator

Board of Pardons and Parole

		Term Expires
Kenneth Peterson	Chair	1/1/2007
John Red	Member	1/1/2007
Melbert Eaglefeathers	Member	1/1/2009
Margaret Hall	Member	1/1/2010
Daryl Dupuis	Auxiliary Member	1/1/2010
Don Hargrove	Auxiliary Member	1/1/2007
Vance Curtess	Auxiliary Member	1/1/2009
Teresa McCann O'Connor	Auxiliary Member	1/1/2009

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Department of Corrections

This financial-compliance audit report contains the results of our audit of the Department of Corrections for the two fiscal years ended June 30, 2006. We issued an unqualified opinion on the financial schedules contained in this report. This means the reader can rely on the financial information presented and the supporting detailed information on the state's accounting records.

This report contains twelve recommendations. The recommendations relate to the department's control structure, various aspects of financial accountability, monitoring and administration of contracts, contractor payments, and compliance with state laws.

The prior audit report contained four recommendations. The department implemented one recommendation, partially implemented two recommendations, and did not implement one recommendation. The audit recommendation not implemented relates to training requirements for probation and parole officers.

The listing below serves as a means of summarizing the recommendations contained in the report, the department's response thereto, and a reference to the supporting comments.

Department Response: Concur. See page B-3.

Department Response: Concur. See page B-3.

Introduction

Introduction and Scope

We performed a financial-compliance audit of the Department of Corrections (department) for the two fiscal years ended June 30, 2006. The objectives of the audit were to:

1. Obtain an understanding of the department's control systems and, if appropriate, make recommendations for the improvement of management and internal controls of the department.
2. Determine if the department complied with selected laws and regulations.
3. Determine the implementation status of recommendations made in the prior audit.
4. Determine if the department's financial schedules present fairly, in accordance with state accounting policy, the results of operations for the audit period.

This report contains twelve recommendations to the department. Areas of concern deemed not to have a significant effect on the successful operation of department programs are not specifically included in the report but have been discussed with management. In accordance with section 5-13-307(2), MCA, we analyzed and disclosed the cost, if significant, of implementing the recommendations in this report.

As required by section 17-8-101(6), MCA, we reviewed and are reporting on the reasonableness of Internal Service Fund fees and fund equity balances at the department. We reviewed the Internal Service Fund activity of the prison industries training program and determined the rates are commensurate with costs for fiscal year 2004-05 and 2005-06. We also reviewed the Montana State Prison cook/chill operations and determined the rates are not commensurate with costs during the fiscal years 2004-05 and 2005-06 and are discussed on page 24.

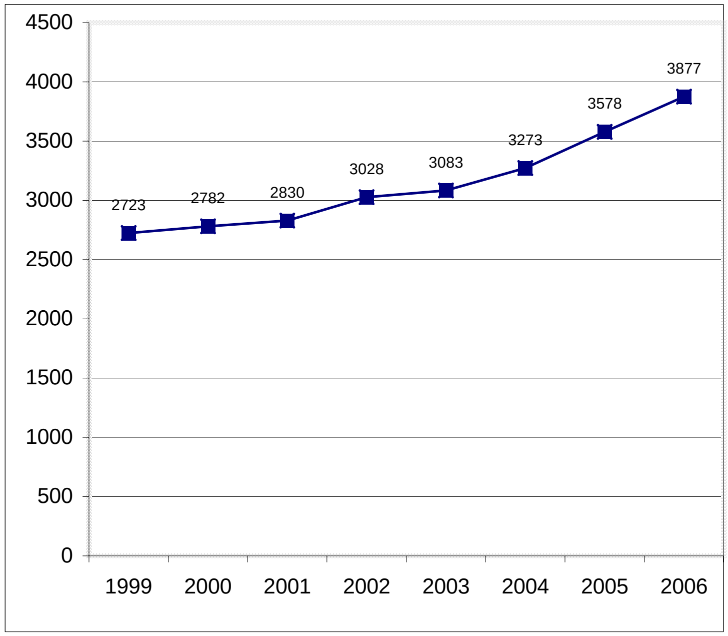
Background

The Department of Corrections promotes public safety and trust by holding adult and juvenile offenders accountable for their actions against victims through custody, supervision, treatment, work, restitution, and skill development.

The Department of Corrections adult male population was 3,402 and adult female population was 475 on June 30, 2006.

Figure 1

Montana's Adult Inmate Population by Fiscal Year



Source: Complied by Legislative Audit Division.

To respond to the need for prison beds, Montana has helped fund three regional prison facilities located in Cascade, Dawson, and Missoula Counties, and has contracted for inmate beds with a private prison located in Shelby. Additionally, the department has expanded community-based programs in the state.

Table 1

Adult Population

MALE PRISON	**FY2005**	**FY2006**
Montana State Prison - Deer Lodge	1,430	1,459
County Jails	125	172
Great Falls Regional Prison	151	151
Dawson County Regional Prison - Glendive	141	142
Crossroads Correctional Center - Shelby	458	501
TOTAL MALE PRISON	**2,305**	**2,425**
% Growth	8%	5%
FEMALE PRISON		
Montana Women's Prison - Billings	186	218
County Jails	44	46
TOTAL FEMALE PRISON	**230**	**264**
% Growth	32%	15%
ALTERNATIVES TO SECURE PLACEMENT / MANAGED BY COMMUNITY CORRECTIONS		
Missoula Assessment and Sanctions Center (male)	133	135
Billings Assessment and Sanctions Center (female)	17	20
TSCTC Boot Camp (male) - Deer Lodge	54	52
Intensive Challenge Program (female) - MWP - Billings	6	15
START (revocations only) - Warm Springs		35
WATCH Program (DUI) - male - Warm Springs / Glendive	119	123
WATCH Program (DUI) - female - Glendive	20	23
TOTAL ALTERNATIVES TO SECURE PLACEMENT	**349**	**402**
% Growth	1%	15%
COMMUNITY CORRECTIONS - PRERELEASE		
Connections Corrections (male) - Butte / Warm Springs	41	67
Connections Corrections (female) - Butte	14	20
Prerelease (male)	472	515
Prerelease (female)	117	120
TOTAL COMMUNITY CORRECTIONS - PRERELEASE	**644**	**722**
% Growth	11%	12%
COMMUNITY CORRECTIONS - PRERELEASE COMMUNITY OPTIONS		
Enhanced Supervision Program Male		4
Enhanced Supervision Program Female		1
Prerelease Transitional Living Male	38	46
Prerelease Transitional Living Female	12	12
TOTAL COMMUNITY CORRECTIONS - PRERELEASE COMMUNITY	**50**	**63**
COMMUNITY CORRECTIONS - INTENSIVE SUPERVISION PROGRAM		
Intensive Supervision Program	288	306
% Growth	13%	6%
COMMUNITY CORRECTIONS - PROBATION & PAROLE		
Probation & Parole	7,073	7,536
% Growth	4%	7%
Growth Total	**10,890**	**11,719**
% Growth	6%	8%
Increase From Previous Year	587	828

Source: Compiled by the Legislative Audit Division and the Department of Corrections.

Introduction

The department currently operates five programs: Administration and Support Services, Adult Community Corrections, Juvenile Corrections, Secure Custody Facilities, and Montana Correctional Enterprises. The following paragraphs describe the organization of the department at June 30, 2006. The budgeted fiscal year 2006-07 full-time equivalent (FTE) numbers listed for each program were obtained from the Legislative Fiscal Division Fiscal Report for the 2007 Biennium and department personnel.

Administration and Support Services

The Administration and Support Services program (97.50 FTE) includes expenditures for the Director's Office; the Health, Planning, and Information Services Division; Administrative and Financial Services Division; Human Resources Division; and the administratively attached Board of Pardons and Parole. The Director's Office provides leadership and management support to all department facilities and divisions. The Director's Office provides quality assurance, investigation, and victim's information. The Human Resources Division provides training and policy functions. The Board of Pardons and Parole oversees Montana's inmate parole and furlough programs. The board also reviews requests for executive clemency and makes recommendations to the Governor concerning those requests.

On April 21, 2006, the department eliminated its Centralized Services Division and replaced it with the Health, Planning, and Information Services Division and the Administrative and Financial Services Division. The Health, Planning, and Information Services Division includes the health services, information and business technology, and the planning management bureaus. The Administrative and Financial Services Division focuses primarily on agency budgeting, procurement, contracting, and many other fiscal responsibilities.

Community Corrections

The Community Corrections program (224 FTE) includes expenditures for the supervision and alternative activities for adult offenders, including the Interstate Compact Unit, Adult Probation and Parole, Treasure State Correctional Training Center, Warm

Springs Addiction Treatment and Change (WATCh) DUI facility, and the Adult Prerelease Unit. On December 12, 2005, the department began the START program for "technical" violations only. Community Corrections provides supervision for approximately 75 percent of the more than 10,000 adult offenders in the state correctional system.

Youth Services

The Youth Services Division (202.85 FTE) includes expenditures for all state operated youth programs, including the Pine Hills Youth Correctional Facility in Miles City, Riverside Youth Correctional Facility in Boulder, and Youth Community Corrections Bureau, including parole services and youth transition centers. The program is also responsible for administering the Juvenile Interstate Compact for youth on probation or parole, licensing juvenile detention facilities, and juvenile placement related financial services.

Secure Custody Facilities

The Secure Custody Facilities program (630.79 FTE) includes expenditures for the Montana State Prison (MSP), Montana Women's Prison (MWP), and contract facilities, including the Crossroads Correctional Center in Shelby, Cascade and Dawson County Regional Prisons, and Missoula Assessment and Sanctions Center. These facilities provide for the custody, treatment, training, and rehabilitation of about 25 percent of the more than 10,000 adult offenders in the state correctional system. Facility locations include Missoula, Great Falls, Glendive, Shelby, Billings, and Deer Lodge.

Montana Correctional Enterprise

The Montana Correctional Enterprise (MCE) program (78 FTE) includes expenditures of the ranch, dairy, and vocational training and industries activities. The ranch and dairy provide dairy products to state institutions and beef cattle, grain, and surplus raw milk to the open market. The vocational/training program provides equipment and vehicle repair to state agencies and vocational education programs. The industries program provides manufactured products (furniture, upholstery, print, signs, and license plates) to state agencies and local governments. A local dealer network is used to sell products manufactured by inmates. On July 1, 2005, the canteen and food services moved from the Secure Custody Facility program to the MCE program.

Prior Audit Recommendations

Our previous audit report for the department, covering the two fiscal years ended June 30, 2004, contained four recommendations. The department concurred with all the recommendations in the previous report. Of these recommendations, the department implemented one of the recommendations, partially implemented two of the recommendations, and did not implement one recommendation.

The department has not implemented controls to ensure probation and parole officers receive the training required by state law and department policy. This is discussed on page 28.

The department did not complete all recommended adjusting entries to accounts receivable on the accounting system. This is discussed on page 13.

The department has made improvements to ensure contracts are signed in a timely manner. However, some contracts were not signed timely and the department did not properly bid out contracts over $25,000. This is discussed on page 17. Recommendations related to contracts have been in the previous four prior audit reports.

Findings and Recommendations

Controls and Compliance

Control structures include identifying risks to achieving management's control objectives and determining how to manage them; applying policies and procedures to ensure management and accounting directives are carried out; informing and communicating methods used to record, process, summarize, and report an organization's financial transactions; and assessing the quality of the control structure over time.

This audit report contains issues related to financial accountability, contract administration, and compliance issues. We believe many of the issues in this audit report may have been prevented or detected and corrected in a timely manner if the department had a more effective communication and training component within its control structure.

Correcting the individual issues identified in this report will not address the underlying cause. The department should implement an effective control structure that addresses the elements described above, with specific emphasis on training and communication.

Recommendation #1
We recommend the department develop a control structure, with an emphasis on training and communication, to help prevent or detect and correct financial and compliance issues.

Financial Accountability

Department operations are primarily funded with state General Fund appropriations, some State and Federal Special Revenue Fund moneys, and Enterprise Fund moneys. During the course of the audit, we identified areas of concern related to the department's financial accountability over these funding sources and how personnel recorded activity on the accounting records. The following report sections discuss our findings.

Unrecorded Revenues and Expenditures

The department did not record all revenues and expenditures on the state's accounting system.

During the audit we found instances where the department reduced expenditures instead of recording revenue and, in other instances, the department recorded receivables instead of revenues and expenditures. The following instances caused an understatement of revenues and expenditures on the states accounting records. State law and accounting policy require the department to report the receipt, use, and disposition of all public money and property in accordance with generally accepted accounting principles. State policy requires recurring expenditures incurred for the convenience of an outside party, who later reimburses the agency, to record the activity as revenues and expenditures. The department should budget for these revenues and expenditures.

Training

The department develops and provides training and training manuals to department employees and other individuals throughout the year. Charges to outside parties for these services are recorded as a receivable. When the services are provided the department reduces the receivable and increases cash when it receives reimbursement. When all transactions have processed there is no longer any outside party training activity recorded on the department's records. We estimate revenues and expenditures for training and manuals are understated by approximately $26,000 for both fiscal years 2004-05 and 2005-06 through March 2006.

Department personnel indicated they used this procedure because they did not believe they had to record cost and expenses of an outside party on their books. They stated it would take up the department's training budget to pay for an outside party's training. However, state accounting policy specifically addresses this situation. Because this activity is recurring, it should be included in the budget for both the revenues and expenditures.

Bus Transportation

In fiscal year 2005-06 the department entered into a contract with a bus company to provide transportation for correctional officers to and from the Montana State Prison. The correctional officers who use the service are charged a per trip fee. The amount the officers pay does not cover the full cost of the transportation. The department pays the remaining costs as specified by the contract. The contract price is based on a set weekly rate. The department recorded the difference between collections from the officers and the weekly contract rate as an expenditure on the accounting records. During the course of the fiscal year, revenues and expenditures were not recorded for the amount collected from the correctional officers. We estimate that revenues and expenditures are understated approximately $44,000 in fiscal year 2005-06.

Department personnel stated they did not realize they should record the officers' payments as revenue. They believed only the state funded portion of the contract rate should be recorded on their records. However, the department is responsible for paying the weekly contract rate regardless of whether the service is used or whether there is a fee charged to the users. The department should record revenue and expenditures from the fees collected from the correctional officers. After we discussed this with the department, a correcting entry was made to record the revenue and expenditures prior to the close of the books for fiscal year 2005-06.

Medical Co-payments and Deductibles

The department is responsible for providing medical care to individuals in its custody. The department developed a policy requiring some individuals to pay a $2 co-payment when medical services are provided. The department also requires the Crossroads Correctional Center in Shelby to pay a $1,000 per inmate medical deductible. When these services are provided the department pays for the service and records an expenditure. As the department collects the co-payments, the medical expenditures are reduced by the amount of the co-payments and deductibles.

Department personnel stated they believe the payments should be used to help reduce medical costs. Accounting policy states that since this is routine and recurring, the department should record revenue for the payments and the medical expense should not be reduced. We estimate that revenues and expenditures are understated by approximately $124,000 and $162,000 in fiscal years 2004-05 and 2005-06, respectively.

Recommendation #2
We recommend that the department record revenues and expenditures as required by state law and accounting policy.

Inconsistent Accounting Practices

The department records financial activity inconsistently and inefficiently.

State accounting policy establishes accounts and procedures for state agencies to properly record accounting transactions in an efficient and effective manner. Generally accepted accounting principles require financial activity be recorded consistently.

The department does not always record transactions in an efficient or consistent manner. In certain instances, the department records expenditures and revenues, and later reverses the transaction creating accounts receivable, deferred revenues, accrued expenditures, liabilities, or fund changes. While reviewing accounting transactions we found this type of accounting common. The department processed approximately 89,000 transactions in fiscal year 2003-04, 91,000 transactions in fiscal year 2004-05, and 97,000 transactions in fiscal year 2005-06 for revenues and expenditures. The increase in transactions is not supported by new activity within the department. The following are some examples of inefficient and inconsistent transactions.

- Department personnel did not want to create negative cash balances in the Federal Special Revenue Fund and there were delays getting cash reimbursements, so they recorded revenues and expenditures, then in some instances, removed them and recorded either deferred revenue, accounts receivable, accruals, or recorded expenditures in the General Fund.
- The department discontinued using the state's accounting system for tracking restitution. To remove the activity from the

accounting system the department removed the accounts receivable and the related liability. However, the department used two different liability accounts. This made it difficult and complicated to remove the activity and it created errors, as discussed on page 13.

- In one instance the department moved all activity in one program to another program. The department removed all activity from the old program by recording receivables and uncleared collections. The department then attempted to clear these accounts and record the transactions in the new program. This created many errors and over 10 journals to move all of the activity.

- The department eliminated certain training costs from its accounting records as discussed on page 8. When costs were originally incurred personnel recorded them using other accounts receivable or expenditure accounts. Department personnel stated they were told to use receivables and cash. However, we found that sometimes expenditure accounts were also used. Most transactions we reviewed were not consistently recorded, which increases the risk of undetected errors. Department personnel stated they use receivables and cash when no specific expenditures were incurred. They used expenditures for specific purchased items and when payment was received they removed the expenditure.

During the audit we found it difficult to determine if account balances were accurate, if accounts were used properly, and if all activity eventually was recorded properly. In some cases review of a single transaction required assessing the validity of many correcting and adjusting accounting documents to determine whether a transaction was ultimately recorded in the proper account and fund. In other instances, we had to discuss the issues with accounting personnel and draw flow-charts to determine if the transactions were reasonable. This took a great deal of time for both department personnel and audit staff. Department personnel stated they were processing transactions the way they were trained. They stated they did not want negative cash situations, and some correcting transactions were input by different personnel.

The department should review its transactions processing methodologies and develop processes that allow staff to perform their work efficiently, effectively, and consistently, thus minimizing the number of corrections and adjustments needed. Increased communications and training would assist this process by providing staff efficient and effective ways to record and process transactions.

<u>Recommendation #3</u>
We recommend the department establish policies and procedures, increase communication, and train staff to provide for consistent and efficient transaction processing.

Control Weaknesses and Accounting Errors

The department made errors in recording financial activity and did not have proper controls in place to prevent or detect and correct errors.

State law requires the Department of Administration to prescribe and install a uniform accounting and reporting system for all state agencies to report the receipt, use, and disposition of all public money and property in accordance with generally accepted accounting principles. The Department of Administration has developed an accounting system and policies and procedures to help ensure state agencies are recording transactions correctly. They are also available to answer questions from other departments.

The department has developed controls intended to ensure personnel record revenues and expenditures appropriately. Some of the controls developed were not effective, and as a result accounting errors occurred and were undetected by department personnel. The following is a list of items we noted.

- Montana Correctional Enterprises (MCE) started a federal certified program in fiscal year 2005-06, which allows inmates to work at higher paying wages. State law allows the department to collect room and board charges from the inmates that work in this program. Federal regulations allow the department to partially recover room and board costs. Room and board expenditures are paid with General Fund moneys. The department recorded the reimbursement in the MCE Enterprise Fund. The department recorded the room and board costs in the wrong fund. Department personnel stated federal guidelines allow them to take money out for room and board, and these guidelines say the revenues are to be used to defray the costs of incarceration. By recording them in the MCE fund they believe they are meeting the requirements. However, initial room and board are paid from the General Fund, so the reimbursement should be recorded in the General Fund. General Fund revenues are understated $20,328 and Enterprise Fund revenues are overstated by the same amount in fiscal year 2005-06. The revenue should be transferred to the General Fund.

- MCE allocates indirect costs to its cannery activity. State policy requires the department to send a proposal detailing the indirect cost allocation on a yearly basis to the Montana Food Bank. The department was unable to support the amounts of indirect costs allocated to the cannery, and has not sent a yearly updated proposal to the food bank. Department personnel stated the rate they were charging has not changed since they started the cannery.
- To track customer orders and shipments, MCE maintains sequential ticket numbers for industries, the dairy, motor vehicle maintenance, and the food service. We found approximately 40 missing tickets of a total of 14,883 tickets during fiscal years 2004-05 and 2005-06. The department did not follow up on these missing tickets. Missing tickets indicate the department was unable to bill for items and revenues may be understated. Department personnel stated they should be following up on all missing tickets, but sometimes it is difficult to get individuals to provide the information.
- The department has many noncurrent balances in its receivable accounts. During the previous audit there was an audit recommendation related to outstanding receivables. We found the receivables related to the previous audit recommendation were not updated. The balance is approximately $248,970 at June 30, 2006. In addition, we found other outstanding receivables. The department adjusted most of the other outstanding balances or made attempts to collect the amounts late in fiscal year-end 2005-06, after we discussed the issue with department personnel.
- The department was using the state's accounting system to record offender restitution balances and payments. It determined the system was not effective. The department attempted to clear the receivables originally recorded, but did not verify the receivable balance. We noted balances still existed in two accounts, which this caused an overstatement of

receivables of $385,784 at fiscal year end 2004-05. Fiscal year 2005-06 balances were corrected after we discussed the issue with personnel.

- The department relies on contractor's bills to determine the reasonableness of pharmacy and medical payments. The department does not have effective controls in place to verify whether or not medical services were provided to individuals before paying for medical services. The department also did not have procedures in place to ensure pharmacy charges were accurate. These are some of the larger expenditures of the department. In both fiscal years 2004-05 and 2005-06 expenditures were $3.3 million and $2.2 million for medical and pharmacy expenditures, respectively. The department is working on implementing new procedures after the issues were discussed with audit staff.
- The Montana State Prison pays the industries training program for motor vehicle repairs. The prison pre-pays for the repairs. These payments should be recorded as a prepaid expense until specific repairs are done. However, the prison records the full expenditure when it pre-pays. The prison paid $37,285 and $38,688 in fiscal years 2004-05 and 2005-06, respectively. The department's expenditures are overstated and assets understated by the amounts of the pre-payment until the services are fully. Department personnel stated it had always been done this way, and did not know it was incorrect.
- The department does a quarterly review to compare shift logs to timesheets. During the audit, we reviewed the process and found errors not identified by the review. We found overtime paid but not recorded on the shift log; timesheets not signed; shift logs indicating leave and timesheets did not match; timesheets on the log were not tested; lack of documentation that the review was done; timesheets in the review did not correspond to the work log; and shift logs were missing so the reviews were not done. The department indicated that issues identified during the reviews are referred to the command post at the Montana State Prison. However, the command post does not have additional information or documentation to resolve the issues. Failure to appropriately resolve identified issues and failure to perform the reviews makes the control ineffective and increases the risk of inappropriate and erroneous payments to employees.
- The department is responsible for maintaining accounts holding inmate funds. It is also responsible for paying inmates on a timely basis. One bank account is used for all inmate moneys. A separate system is used to track individual inmate balances in

the account. One regional prison we visited indicated payments to the bank account were not timely. This caused problems with inmates and inmate purchases. To avoid problems the prison credited the individual inmate accounts even though the money was not in the bank account. This overstates inmate account balances and allows the inmates to spend money that was not actually available. Department personnel stated this was done because inmate payroll was not timely and inmates were frustrated.

- The department receives several federal grants where moneys are received in advance of expenditures being incurred. Federal guidelines require the recipients to minimize the time elapsing between the transfer of funds and disbursement. Federal guidelines state that advances must be the minimum amount needed in that month for carrying out the purpose of the approved project. We found the department requested advances for entire grant amounts, or sometimes a portion larger than needed. We found three instances where the department requested advances and did not spend the money in a timely manner. This caused cash balances to be higher than necessary.
- The department receives several federal grants where it is reimbursed for expenditures incurred. We found instances where the department used General Fund money to pay initial expenditures and did not request federal reimbursement in a timely manner. We noted instances where reimbursements were requested quarterly although funds are available either immediately or at least monthly. As an example, the department incurred expenditures $8,964 from December 2005 until June 2006, which were paid by the General Fund until reimbursement was received in June. Department personnel stated the reimbursement process was difficult, so they tended to request funds less often.

The number and types of errors indicate the department does not have an effective control structure in place. The department should implement an adequate control system for its accounting transactions to help detect and correct accounting errors and to ensure they are following policy and accounting principles. Increased training of staff entering transactions and additional communication between staff will help implement controls.

Recommendation #4

We recommend the department implement controls to prevent and detect and correct accounting errors on a timely basis.

Livestock Valuation

The department does not record livestock assets according to state policy.

The department's recorded livestock inventory balances were $4,027,049 and $3,692,555 at June 30, 2006 and 2005, respectively. State accounting policy requires the department's livestock be valued and recorded on the accounting records based on established industry practice and generally accepted accounting principles. These accounting requirements state that all costs of acquiring and raising animals should be accumulated until the animals reach maturity and are transferred.

Depending on the classification, the accounting for the matured animals can be different. In simple terms, livestock held for breeding, dairy, or not available for sale, should be classified as fixed asset and potentially depreciated over their useful life. Livestock are considered available for sale when they are available for immediate delivery. Livestock that meet the available for sale criteria should be recorded in livestock inventory. Animals not available for immediate delivery should not be recorded as livestock inventory.

The department records all livestock, including dairy and breeding cattle, in the livestock inventory account. At year-end the department uses revenues from a few cattle sales to determine an average price through-out the year. It multiplies the average by the number of livestock and records the computed value as livestock inventory. This indicates all ranch livestock will be sold immediately, which would leave the ranch with no productive assets.

The department does not track accumulated costs, record fixed assets, or depreciate the mature cattle used for dairy and breeding. This results in an understatement of expenditures, depreciation, and capitalized livestock and an overstatement of livestock inventory.

Department personnel stated that the way they record livestock was in accordance with state policy developed by the Department of Administration. We were unable to locate a copy of the policy, however, the Department of Administration stated that the policy no longer applies, but an alternative policy now exists. This policy requires the Montana State Prison ranch follow generally accepted accounting principles when recording livestock assets. The department should review its accounting procedures to ensure it complies with state accounting policy for recording livestock assets.

Recommendation #5
We recommend the department ensure Montana Correctional Enterprise's ranch livestock assets are recorded in accordance with state policy.

Contract Administration and Monitoring

The department does not ensure contracts are signed before the effective date, contracts are bid as required by state law, and contract requirements are met.

We have recommended the department implement and enforce contracting policies and procedures to ensure contracts are signed in a timely manner in each of the four prior audits. The last two audits included recommendations relating to contract bidding procedures. The department has implemented policies related to contracts and contracting that have specifically addressed these recommendations. Department policy states, "The contractor cannot start work prior to signing the contract and the effective date must not occur before the receipt of all contract signatures." During the current audit we noted this was still an issue.

The department does not have effective controls in place to ensure requirements within the contracts are met. Department policy states the goal of a contract is to obtain an agreement between two or more parties that details duties, responsibilities, and compensation terms for all parties involved. In order to ensure this goal is met the department needs to develop effective controls. The following report sections discuss our findings.

Contract Administration

The department enters into contracts both for providing and receiving goods and services. Department policy, as noted above, states that a contractor cannot start work until a signed contract is in place. Department policy requires in most situations contracts over $5,000 be bid. State law requires specific documentation for sole source contracting. During the audit we found contracts that were not in compliance with department policy and state law.

- The department contracts with a boot company for industries training. The original contract expired June 2005. A new contract was signed on November 30, 2005, with an effective date of November 1, 2005.
- The department contracts with a lumber company for industries training. A contract was entered into January 19, 2004, and was not signed until January 26, 2004. On April 4, 2005, the original contract was amended. The amendment was not signed until June 30, 2005. The original contract expired April 4, 2006. The department signed an addendum February 21, 2006; however, it did not extend the length of the contract. As of June 30, 2006, the contract has not been renewed. The department is using the expired contract to continue the program.
- The department contracts with a substance abuse counselor. The contract had an effective date of November 1, 2004. The department signed the contract November 22, 2004, and the contractor signed on December 8, 2004.
- The department did not have a valid contract with an individual who provided services to the dairy. A valid contract was not signed until May 2006. Expenditures of $10,440 and $10,601 were paid in fiscal years 2004-05 and 2005-06, respectively, before there was a valid contract.
- The department contracted services for a dam project. One addendum to the contract expired June 30, 2005. A new addendum was not signed until May 2006. The department paid the contractor $24,416 during the time period when no valid contract existed.
- The department contracts with a dairy nutritional consultant. The original contract expired April 2005 and an addendum was

not signed until June 2006. The department paid expenditures of $8,283 on an expired contract.

- In the prior audit it was determined that a medical services contract should go out for bid. During the current audit we noticed the contract has not yet been bid.
- We tested three sole sources contracts, and found two of the contracts did not comply with state law. Department personnel did not appropriately document they were unable to find other sources for the services. Based on our review they should not have been sole source contracts.

Department personnel stated the boot program became a federal program on November 1, 2005, so they chose not to renew the contract until they had federal approval. According to department personnel, the other contract issues were oversight, and they have worked to improve contract issues. They added that in previous audits, very few contract renewals were timely, and they have worked hard at ensuring most contracts are now following state law and policy. We did note an improvement in the department's procedures. We believe the department should further improve its controls over administration of contracts. Increased communication and monitoring of contracts would improve current controls.

Contract Monitoring

Contracts are developed to obtain legal agreements that detail specific requirements between parties relating to duties, responsibilities, and compensation for purchasing and receiving goods or services. Standard contracts contain language requiring the contractor to follow various laws and policies the department is required to follow. Monitoring contracts decreases the department's potential liability, ensures the department is receiving or purchasing appropriate goods and services, ensures the department is following state law and policy, and is necessary to determine compensation amounts. Therefore, it is important for management to develop controls to ensure compliance with contracts entered into by the department. During the audit we found instances where either the department or the contractor were not in compliance with contract requirements.

- The department has a lumber contract which states the department will charge based on input board footage. The department verbally agreed to charge based on output board footage for approximately six months in fiscal year 2005-06. This resulted in the department losing $17,698 in revenues. Department personnel stated they used the verbal agreement to make changes because the lumber company was not making a profit and was considering discontinuing the contract.
- The department contracts with pre-release centers throughout the state. Many of the contracts require the department to reduce payments to the centers for principle and interest amounts due on bonds coming due in the following 12 months. The department is responsible for making the bond payment to the bond trustees. An updated version of a bond for one facility was received in August 2005, but the department did not recalculate current bond principle and interest amounts to adjust payment amounts. The department's documentation showed current bond payments should have been $25,031 a month, however the department used prior year amounts and was paying $17,304 a month. When we brought this to the department's attention an adjustment was made before year-end.
- The private prison contract requires the private prison to pay $1000 per inmate per year for medical deductibles. One of the facilities has not been billed for the medical deductibles since January 2006. Department personnel stated they keep a spreadsheet to bill these amounts, but were behind on updating the spreadsheet.
- Contract provisions at the private prison require the prison to receive authorization from the department for scheduled non-emergency medical costs exceeding $1,000. The contract states that the department will not pay for medical services that were not approved. The private prison does not get approval, but the department has paid for medical services that are not its responsibility. Individuals at the private prison stated approval is given from the prison's medical director, and the department had indicated to them that was sufficient approval.
- Department policy and contracts with regional prisons require eligible inmates to pay a $2 co-pay for medical services. Some of the regional prisons remit the co-pay, some remit sometimes, and others do not remit at all. The department does not track the amounts owed from the regional prisons and does not record and collect the moneys to which it is entitled under contract. The department has not clearly communicated and enforced the co-pay provision.

- Regional prison contracts make the prison responsible for inmate dental care. Personnel at one regional prison we visited stated that they are unable to provide routine dental care for the inmates. Personnel stated they are unable to hire a dental hygienist and the number of inmates requiring major dental work has recently increased.

In addition to the specific items noted above, we found many contracts included: incorrect state law references, repealed laws and policy references, reference to repealed laws and policies and the term of contract was not always included. The department should develop controls to administer and monitor contract compliance. Improved controls should prevent or allow for earlier detection and correction of the types of issues discussed above.

Recommendation #6
We recommend the department implement adequate controls over contract administration.

Contractor Payments

The department paid $25,000 for unsupported contracted services.

The department entered into a contract to determine the feasibility of providing transportation services to department employees. The contract required an operational analysis for providing commercial transportation for department employees to various department facilities and locations. The contract required specific cities to be reviewed, including Butte, Anaconda, Helena, Boulder, Drummond, Deer Lodge, and Missoula. The contract stated, "Contractor will review, analyze, and submit findings and recommendations to the department. Submission of the final report shall occur not later than February 15, 2006." The contract required meetings with key staff, reviewing absolute capacity of commercial transport per shift, analyzing staff surveys, facilitating community plans, and identifying potential childcare opportunities at all of the locations mentioned above. The department was to pay the contractor based upon an hourly rate, not to exceed $25,000, after the receipt of a correct invoice. The contract also had a provision stating, "[the] Department may withhold payments to the contractor if the contractor has not performed in accordance with the terms of this contract."

We reviewed invoices related to the contract. The invoices did not contain hours worked by the contractor. Documentation on the invoices contained questions by department personnel as to whether or not payment should be made and indicated that personnel requested support for the payments. Department personnel stated no additional support was provided. Management responsible for the contract authorized payments. On February 15, 2006, the department received a letter from the contractor describing the work completed to date. The letter did not address the requirements of the contract as stated above. Department personnel asked for support and for a final report as required by the contract. The contractor sent another letter March 7, 2006, indicating the letter should be used for the final report. This additional letter also did not completely address the requirements of the contract. According to department personnel, other attempts to receive a final report were unsuccessful. The department paid the contractor $5,000 a month for a total of $25,000. Final payment was made on March 2, 2006. The payments were made without required support and a final product was not delivered as required by the contract.

We requested, but were unable to obtain, documentation of any review, analysis, or findings and recommendations as required by the contract. We requested and were unable to obtain a final report provided by the contractor. Contract provisions allow the department to withhold payments if the contractor has not performed in accordance with the contract. The department should attempt to enforce the contract or recover the costs and develop controls to ensure requirements of contracts are met before contractors receive payment.

Recommendation #7
We recommend the department:

A. **Enforce the terms of the contract or seek reimbursement from the contractor for $25,000 paid under its transportation study contract.**

B. **Implement controls to ensure documentation required by contracts is received before approving contract payment.**

Retirement Misclassifications

The department enrolled employees in incorrect retirement systems.

State law specifies to which retirement system an employee must belong. Teachers and principals are included in the Teachers' Retirement System (TRS). Correctional officers are active in the Game Wardens' and Peace Officers' Retirement System (GWPORS). Individuals not covered by a separate retirement system and who are employees of the state are included in the Public Employees' Retirement System (PERS). The department contributes to the different retirement systems depending on the employees' classification.

During our audit we found three instances where employees were in incorrect retirement systems.

- One employee was a correctional officer and active in GWPORS. In August of 2003 the individual changed positions and became a teacher, but the department did not change retirement systems. As a teacher, the employee should be an active member of TRS. The contribution rates for TRS are less than for GWPORS. The department and the employee both contributed more than they should towards retirement.
- One employee was a teacher and active in TRS. The employee changed positions and has been a food supervisor since February 2000, which would require the employee to be an active member of PERS. The department did not change retirement systems. The TRS contribution rate is higher than the PERS contribution rate. The department and the employee both contributed more than they should towards retirement.

- One employee was classified as a correctional officer on the system, but the job duties and description were for a principal. The employee was active in the PERS, which corresponds to the position classification, but not to the job duties. We determined the employee should be active in the TRS system. The employee was a retired teacher and was receiving full benefits from TRS. The employee should have been active in TRS, and retirement benefits should have been reduced. The employee was overpaid by the retirement system $15,354 and $14,558 in fiscal years 2004-05 and 2005-06, respectively. Also, the PERS contribution rates are lower than the TRS system. The department and the employee both contributed less than they should towards retirement.

Department personnel stated enrollments in retirement systems for the first two employees discussed were oversights. They said the last individual was classified for state budgeting purposes as a correctional officer, but for accreditation purposes as a principal. According to department personnel, school accreditation was at risk unless a principal was employed. When we discussed this with department personnel, they agreed to correct the classification. The department should implement controls to ensure employees are enrolled in the proper retirement system.

Recommendation #8
We recommend the department ensure its employees are enrolled in the proper retirement systems in accordance with state law.

Internal Service Funds

Fees charged by the department's Internal Service Funds are not approved by the legislature and fees are not commensurate with costs.

State law requires all fees and charges, in the Internal Service Fund (ISF) type, be approved by the legislature in the general appropriations act. State law requires the fees be commensurate with costs. One of the department's ISF's is the Montana State Prison cook/chill operation.

Only some of the fees in the cook/chill program were approved by the legislature. The legislature approved fees for per tray meals at specific facilities. Fees not approved for the cook/chill program include bulk food, extra food, accessory packs, and delivery fees.

We analyzed the revenues and expenses as well as working capital. We found cook/chill operation revenues exceed expenses, and the fund balance is increasing. The ending working capital exceeds a 60-day statutory limit, by approximately $82,166, and $243,245 in fiscal year 2004-05 and 2005-06, respectively.

Table 2

Working Capital (WC)

	July 1 WC	Revenues	Expenditures	June 30 WC
FY 2004-05	$322,233	$2,929,510	$2,886,105	$563,183
FY 2005-06	$563,183	$3,088,548	$3,097,822	$759,549

Source: Compiled by the Legislative Audit Division.

Personnel stated they did not realize all fees needed approval. The department is currently evaluating the fees to determine if any adjustments to the rates are necessary.

Recommendation #9
We recommend the department comply with state law regarding Internal Service Funds fees, charges, and working capital.

Department Policies

The department is not following its process to update policies and not all policies have been communicated to appropriate personnel.

The department has a policy that states:

> "…all department policies will be accessible to all employees, offenders, and public. The department director

> and policy unit will have direct electronic access to all division and facility procedures. All unrestricted policies will be on the department's web site. Department policy will include an applicability clause and the policy unit will be the central repository for all department policy and will have immediate electronic access to current and archived division and facility policy, and designated staff from each division will coordinate with the policy unit to ensure accurate and timely policy development, review, and distribution. All department policy will be reviewed annually and be updated as needed."

The policy also states that designated staff from each division will coordinate with the policy unit to ensure accurate and timely policy development, review, and distribution.

Currently, the department does not follow its process to update policies and procedures. Department personnel stated many policies have not been updated or reviewed since 1996 or 1997. Specific facility policies are not available on the department's web site or immediately available to the policy unit. We found that policies were updated without the key people being involved, and many policies were not signed.

It is important to implement a formal policy updating process so there is less confusion. Currently, the department's policy unit is not aware of all policies. The department allows almost any individual to create or revise policy without the knowledge of others. One example found during the audit follows:

Montana Correctional Enterprises (MCE) has a policy relating to staff housing. There are five housing units located on the Montana State Prison ranch. The policy addresses who is required to live on the ranch as part of their employment, and rental agreements and amounts for those not required to live in a housing unit. The policy also requires lease agreements for all individuals living in the housing units. We found that the original policy had two updates in the last two years. Neither of the updates were signed and individuals responsible for the housing units, as well as the policy unit in the department, were not aware of the changes to the policy. It was not apparent as to why the policies were changed, or whether there was discussion of the changes because not all staff at MCE were advised of the changes. The employee who made changes to the policy added their own position as one that is required to live in one of the housing units as part of their employment.

As part of the audit we question why two individuals are required, per newest version of the policy, to live in the housing units. We were unable to find any documentation other than the policy change that made living on the ranch a requirement of service. We reviewed position descriptions and did not find evidence that the individuals were required to live on the prison ranch. The job duties described did not include any reasons why living at the facility was necessary. In addition, the previous employees in those positions were not required and did not live in the housing units. We noted that all employees living in the housing units, except the two in question, had lease agreements. One individual in question had a new lease agreement signed at the end of the audit period. We believe the individuals should be paying rent. We believe the department should have collected approximately $10,200 in both fiscal years 2004-05 and 2005-06.

Department personnel stated that employees were not willing to pay rent and they believed any director should be required to live in the housing units. However, from our review it did not appear that the policy was updated following the department's own policy and changes to the policy were not supported. There was no evident review of the policy changes and the current process allows instances as noted above to occur.

Department personnel also stated that they are behind in updating policies and reviewing policies. They are aware they were not following the process in place to update policies. They are working at getting the department intranet functioning, so more individuals will have access to policies. The department is responsible for ensuring they are in compliance with policies. The department should update outdated policies, communicate new policies, and distribute current policies to appropriate personnel.

Recommendation #10
We recommend the department update, communicate, and distribute current policies to ensure compliance with its internal policies.

Training

The department does not have adequate controls to ensure probation and parole officers and correctional officers obtain the training required by state law and department policy.

Section 46-23-1003, MCA, requires each probation and parole officer to obtain 16-hours of training specific to the officers' duties. Department policy states that probation and parole officers, correction officers, and direct supervision staff are required to have 40-hours of training, including 16-hours of position specific training.

The department is not following either requirement. The previous audit found the department was not in compliance with these requirements and recommended compliance. We noted the department has hired a new training officer and compliance has improved. However, we tested 19 officers and found ten did not meet the 40-hour or 16-hour training requirements.

At one regional prison, staff stated there is currently no way to track training hours and there is not an effective way to train staff. They believe they would have to pay officers overtime to complete the training requirements. Other sites visited were able to track training hours, but were not in compliance with the number of hours required. The new training officer stated that since August 2005 better controls have been implemented and they are still working on them. The department is responsible for ensuring the officers are properly trained in accordance with state law and policy.

Recommendation #11
We recommend the department continue implementing controls to ensure probation and parole officers and correctional officers receive training required by state law and department policy.

Interstate Compact Council

The legislature failed to appoint a member of the interstate compact council.

Section 46-23-115, MCA, establishes members of the interstate compact council. The council is to include a house member appointed by the speaker of the house and a senate member appointed by the president of the senate.

When a previous member of the council was not re-elected the department contacted the speaker of the house to appoint a new member, but no response was received. Another senate member volunteered for the position, so there are currently, two senate members and no house member on the council.

Department personnel stated they attempted to get the house to appoint a new member, and since no response was received they allowed the senator to be a part of the council. It is the department's responsibility to ensure the appropriate members are appointed to the council.

Recommendation #12
We recommend the department work with the legislature to appoint a member of the House of Representatives to the council as required by section 46-23-1115, MCA.

Independent Auditor’s Report & Department Financial Schedules

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor

Deputy Legislative Auditors:
James Gillett
Jim Pellegrini

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Schedules of Changes in Fund Balances & Property Held in Trust, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Department of Corrections for each of the fiscal years ended June 30, 2005-06, and 2004-05. The information contained in these financial schedules is the responsibility of the department's management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 1, the financial schedules are presented on a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The schedules are not intended to be a complete presentation and disclosure of the department's assets, liabilities, and cash flows.

In our opinion, the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances of the Department of Corrections for each of the fiscal years ended June 30, 2005-06, and 2004-05, in conformity with the basis of accounting described in note 1.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

August 21, 2006

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DEPARTMENT OF CORRECTIONS
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Enterprise Fund	Internal Service Fund	Agency Fund
FUND BALANCE: July 1, 2005	$ (7,030,835)	$ 1,101,676	$ (782)	$ 12,282,142	$ 3,930,614	$ 0
PROPERTY HELD IN TRUST: July 1, 2005						$ 823,044
ADDITIONS						
Budgeted Revenues & Transfers-In	95,927	3,720,592	1,100,380	5,717,026	3,462,237	
NonBudgeted Revenues & Transfers-In	10,926	1,195				
Prior Year Revenues & Transfers-In Adjustments	456	78,769	(823)			
Direct Entries to Fund Balance	131,337,851	56,894	(3,911)	(543,033)		
Additions to Property Held in Trust						6,620,582
Total Additions	131,445,160	3,857,450	1,095,646	5,173,993	3,462,237	6,620,582
REDUCTIONS						
Budgeted Expenditures & Transfers-Out	130,792,775	3,500,537	1,096,060	5,083,037	3,307,540	
NonBudgeted Expenditures & Transfers-Out	6,912	130		(242,870)	223,122	
Prior Year Expenditures & Transfers-Out Adjustments	347,655	26,376	(823)		(21,424)	
Reductions in Property Held in Trust						6,771,629
Total Reductions	131,147,342	3,527,043	1,095,237	4,840,167	3,509,238	6,771,629
FUND BALANCE: June 30, 2006	$ (6,733,017)	$ 1,432,083	$ (373)	$ 12,615,968	$ 3,883,613	$ 0
PROPERTY HELD IN TRUST: June 30, 2006						$ 671,997

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF CORRECTIONS
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Enterprise Fund	Internal Service Fund	Agency Fund
FUND BALANCE: July 1, 2004	$ (5,620,103)	$ 703,592	$ 0	$ 12,311,252	$ 3,896,742	$ 0
PROPERTY HELD IN TRUST: July 1, 2004						$ 1,056,170
ADDITIONS						
Budgeted Revenues & Transfers-In	53,584	3,529,816	2,026,944	5,233,926	3,318,362	
NonBudgeted Revenues & Transfers-In	(69,716)	465				
Prior Year Revenues & Transfers-In Adjustments	77,804	334,514	(5,911)			
Direct Entries to Fund Balance	109,355,014	93,891	1,067,212	(561,142)		
Additions to Property Held in Trust						7,668,123
Total Additions	109,416,686	3,958,686	3,088,245	4,672,784	3,318,362	7,668,123
REDUCTIONS						
Budgeted Expenditures & Transfers-Out	110,766,574	3,557,549	3,094,938	4,740,339	2,994,981	
NonBudgeted Expenditures & Transfers-Out	(51,808)			(38,445)	290,651	
Prior Year Expenditures & Transfers-Out Adjustments	112,652	3,052	(5,911)		(1,142)	
Reductions in Property Held in Trust						7,901,249
Total Reductions	110,827,418	3,560,601	3,089,027	4,701,894	3,284,490	7,901,249
FUND BALANCE: June 30, 2005	$ (7,030,835)	$ 1,101,677	$ (782)	$ 12,282,142	$ 3,930,614	$ 0
PROPERTY HELD IN TRUST: June 30, 2005						$ 823,044

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF CORRECTIONS
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Enterprise Fund	Internal Service Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS						
Taxes	$ 4,018	$ 1,195				$ 5,213
Charges for Services		1,489,668		$ 17,283		1,506,951
Sale of Documents, Merchandise and Property		1,318,307		5,699,743	$ 3,462,236	10,480,286
Rentals, Leases and Royalties						0
Contributions and Premiums	6,908					6,908
Miscellaneous	96,383	20,455				116,838
Grants, Contracts, Donations and Abandonments		573,888				573,888
Other Financing Sources		397,043				397,043
Federal			$ 1,099,557			1,099,557
Total Revenues & Transfers-In	107,309	3,800,556	1,099,557	5,717,026	3,462,236	14,186,684
Less: Nonbudgeted Revenues & Transfers-In	10,926	1,195				12,121
Prior Year Revenues & Transfers-In Adjustments	456	78,769	(823)			78,402
Actual Budgeted Revenues & Transfers-In	95,927	3,720,592	1,100,380	5,717,026	3,462,236	14,096,161
Estimated Revenues & Transfers-In	28,299	5,226,840	1,853,434	5,700,000	6,170,000	18,978,573
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 67,628	$ (1,506,248)	$ (753,054)	$ 17,026	$ (2,707,764)	$ (4,882,412)
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS						
Charges for Services		$ 59,351		$ (12,717)		46,634
Sale of Documents, Merchandise and Property		(1,315,329)		29,743	$ (2,707,764)	(3,993,350)
Miscellaneous	$ 67,628	(4,911)				62,717
Grants, Contracts, Donations and Abandonments		(364,181)				(364,181)
Other Financing Sources		118,822				118,822
Federal			$ (753,054)			(753,054)
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 67,628	$ (1,506,248)	$ (753,054)	$ 17,026	$ (2,707,764)	$ (4,882,412)

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF CORRECTIONS
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Enterprise Fund	Internal Service Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS						
Taxes	$ 3,478	$ 465				$ 3,943
Charges for Services		1,519,730				1,519,730
Sale of Documents, Merchandise and Property		1,216,938		$ 5,232,351	$ 3,318,362	9,767,651
Rentals, Leases and Royalties				1,575		1,575
Miscellaneous	58,194					58,194
Grants, Contracts, Donations and Abandonments		705,913				705,913
Other Financing Sources		421,749				421,749
Federal			$ 2,021,033			2,021,033
Total Revenues & Transfers-In	61,672	3,864,795	2,021,033	5,233,926	3,318,362	14,499,788
Less: Nonbudgeted Revenues & Transfers-In	(69,716)	465				(69,251)
Prior Year Revenues & Transfers-In Adjustments	77,804	334,514	(5,911)			406,407
Actual Budgeted Revenues & Transfers-In	53,584	3,529,816	2,026,944	5,233,926	3,318,362	14,162,632
Estimated Revenues & Transfers-In	155,000	4,696,169	2,431,893	10,411,575	6,140,000	23,834,637
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ (101,416)	$ (1,166,353)	$ (404,949)	$ (5,177,649)	$ (2,821,638)	$ (9,672,005)
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS						
Charges for Services	$ (105,000)	$ 64,601	$ (70,439)	$ (575,000)		(685,838)
Sale of Documents, Merchandise and Property		(204,301)		(4,592,649)	$ (2,821,638)	(7,618,588)
Rentals, Leases and Royalties				(10,000)		(10,000)
Miscellaneous	3,584	(307,115)				(303,531)
Grants, Contracts, Donations and Abandonments		(479,766)				(479,766)
Other Financing Sources		(239,772)				(239,772)
Federal			(334,510)			(334,510)
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ (101,416)	$ (1,166,353)	$ (404,949)	$ (5,177,649)	$ (2,821,638)	$ (9,672,005)

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF CORRECTIONS
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

	Administration & Support Services	Community Corrections	Juvenile Corrections	Montana Correctional Enterprises	Secure Custody Facilities	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT						
Personal Services						
Salaries	$ 4,147,509	$ 7,990,117	$ 6,956,325	$ 2,447,865	$ 21,093,599	$ 42,635,415
Hourly Wages	33,411		29,383	446,218	288,146	797,158
Other Compensation	24,005					24,005
Employee Benefits	1,230,846	2,890,642	2,460,834	853,077	7,644,950	15,080,349
Personal Services-Other				41,404		41,404
Total	5,435,771	10,880,759	9,446,542	3,788,564	29,026,695	58,578,331
Operating Expenses						
Other Services	5,787,339	20,269,195	815,746	90,367	27,663,995	54,626,642
Supplies & Materials	906,637	577,817	931,152	5,605,014	4,917,204	12,937,824
Communications	198,355	243,815	94,526	18,563	227,605	782,864
Travel	157,790	108,523	95,246	25,571	122,787	509,917
Rent	359,148	1,248,050	175,425	16,070	140,572	1,939,265
Utilities	862	46,464	373,203	303,337	1,231,165	1,955,031
Repair & Maintenance	96,706	65,887	73,777	476,438	287,802	1,000,610
Other Expenses	296,282	69,700	59,708	559,597	208,857	1,194,144
Goods Purchased For Resale			3,594	4,265,030		4,268,624
Total	7,803,119	22,629,451	2,622,377	11,359,987	34,799,987	79,214,921
Equipment & Intangible Assets						
Equipment			6,500		250,598	257,098
Total			6,500		250,598	257,098
Capital Outlay						
Buildings				(532,058)		(532,058)
Total				(532,058)		(532,058)
Benefits & Claims						
From State Sources			4,490,869			4,490,869
From Federal Sources			(4,320)			(4,320)
Total			4,486,549			4,486,549
Transfers						
Accounting Entity Transfers			1,897,479			1,897,479
Total			1,897,479			1,897,479
Debt Service						
Capital Leases				216,706		216,706
Total			0	216,706		216,706
Total Expenditures & Transfers-Out	$ 13,238,890	$ 33,510,210	$ 18,459,447	$ 14,833,199	$ 64,077,280	$ 144,119,026
EXPENDITURES & TRANSFERS-OUT BY FUND						
General Fund	$ 12,353,718	$ 32,998,342	$ 16,664,128	$ 5,273,006	$ 63,858,148	$ 131,147,342
State Special Revenue Fund	753,185	511,869	871,340	1,264,037	126,612	3,527,043
Federal Special Revenue Fund	78,737		923,980		92,520	1,095,237
Enterprise Fund	47,694			4,792,473		4,840,167
Internal Service Fund	5,555			3,503,683		3,509,238
Total Expenditures & Transfers-Out	13,238,889	33,510,211	18,459,448	14,833,199	64,077,280	144,119,027
Less: Nonbudgeted Expenditures & Transfers-Out	130	545	2,566	(19,748)	3,801	(12,706)
Prior Year Expenditures & Transfers-Out Adjustments	92,481	(10,827)	16,117	(21,424)	275,437	351,784
Actual Budgeted Expenditures & Transfers-Out	13,146,278	33,520,493	18,440,765	14,874,371	63,798,042	143,779,949
Budget Authority	13,397,753	33,706,779	19,152,215	16,748,708	64,381,441	147,386,896
Unspent Budget Authority	$ 251,475	$ 186,286	$ 711,450	$ 1,874,337	$ 583,399	$ 3,606,947
UNSPENT BUDGET AUTHORITY BY FUND						
General Fund	$ 75,041	$ 43,152	$ 73,306	$ 339,521	$ 423,258	$ 954,278
State Special Revenue Fund	78,651	143,134	205,847	45,314		472,946
Federal Special Revenue Fund	94,753		432,297		160,141	687,191
Enterprise Fund	3,030			1,147,026		1,150,056
Internal Service Fund				342,476		342,476
Unspent Budget Authority	$ 251,475	$ 186,286	$ 711,450	$ 1,874,337	$ 583,399	$ 3,606,947

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF CORRECTIONS
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	Administration and Support Services	Community Corrections	Juvenile Corrections	Correctional Enterprises	Secure Custody Facilities	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT						
Personal Services						
Salaries	$ 3,572,763	$ 7,144,480	$ 6,750,718	$ 1,716,494	$ 19,197,979	$ 38,382,434
Hourly Wages	9,755		20,421	329,278	319,773	679,227
Other Compensation	22,600					22,600
Employee Benefits	1,074,885	2,532,592	2,330,691	550,210	6,757,046	13,245,424
Personal Services-Other				(11,639)	1,803	(9,836)
Total	4,680,003	9,677,072	9,101,830	2,584,343	26,276,601	52,319,849
Operating Expenses						
Other Services	6,230,431	16,141,081	1,333,895	73,788	24,243,505	48,022,700
Supplies & Materials	652,217	356,764	804,103	1,888,042	6,028,668	9,729,794
Communications	104,729	207,536	74,688	21,087	199,465	607,505
Travel	129,431	88,862	106,699	16,623	93,214	434,829
Rent	246,047	1,188,879	175,387	17,746	138,192	1,766,251
Utilities		71,314	321,740	226,880	1,180,086	1,800,020
Repair & Maintenance	83,110	63,447	91,627	329,601	318,047	885,833
Other Expenses	244,389	51,712	59,577	1,015,861	478,809	1,850,348
Goods Purchased For Resale			4,167	762,422	1,153,608	1,920,197
Total	7,690,354	18,169,595	2,971,883	4,352,050	33,833,594	67,017,476
Equipment & Intangible Assets						
Equipment	12,968				121,603	134,571
Total	12,968				121,603	134,571
Capital Outlay						
Buildings				(566,793)		(566,793)
Total				(566,793)		(566,793)
Benefits & Claims						
From State Sources			4,141,230			4,141,230
From Federal Sources			26,025			26,025
Total			4,167,255			4,167,255
Transfers						
Accounting Entity Transfers			2,099,025			2,099,025
Total			2,099,025			2,099,025
Debt Service						
Loans					75,339	75,339
Capital Leases				216,708		216,708
Total				216,708	75,339	292,047
Total Expenditures & Transfers-Out	$ 12,383,325	$ 27,846,667	$ 18,339,993	$ 6,586,308	$ 60,307,137	$ 125,463,430
EXPENDITURES & TRANSFERS-OUT BY FUND						
General Fund	$ 11,253,131	$ 26,470,206	$ 15,489,706	$ 1,589,813	$ 56,024,562	$ 110,827,418
State Special Revenue Fund	879,461	303,828	1,094,444		1,282,868	3,560,601
Federal Special Revenue Fund	146,979	1,072,633	1,755,843		113,572	3,089,027
Enterprise Fund	84,358			4,617,536		4,701,894
Internal Service Fund	19,396			378,959	2,886,135	3,284,490
Total Expenditures & Transfers-Out	12,383,325	27,846,667	18,339,993	6,586,308	60,307,137	125,463,430
Less: Nonbudgeted Expenditures & Transfers-Out				(25,820)	226,218	200,398
Prior Year Expenditures & Transfers-Out Adjustments	83,745	17,506	13,084	(1,046)	(4,639)	108,650
Actual Budgeted Expenditures & Transfers-Out	12,299,580	27,829,161	18,326,909	6,613,174	60,085,558	125,154,382
Budget Authority	12,775,947	28,355,766	19,568,548	8,336,489	60,742,845	129,779,595
Unspent Budget Authority	$ 476,367	$ 526,605	$ 1,241,639	$ 1,723,315	$ 657,287	$ 4,625,213
UNSPENT BUDGET AUTHORITY BY FUND						
General Fund	$ 303,164	$ 26,605	$ 137,204	$ 32	$ 260,371	$ 727,376
State Special Revenue Fund	53,474	500,000	2,290		151,109	706,873
Federal Special Revenue Fund	119,729		1,102,145	100,000	159,843	1,481,717
Enterprise Fund				1,545,002		1,545,002
Internal Service Fund				78,281	85,964	164,245
Unspent Budget Authority	$ 476,367	$ 526,605	$ 1,241,639	$ 1,723,315	$ 657,287	$ 4,625,213

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

1. Summary of Significant Accounting Policies

Basis of Accounting

The department uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental fund category (General, State Special Revenue, and Federal Special Revenue). In applying the modified accrual basis, the department records:

> Revenues when it receives cash or when receipts are realizable, measurable, earned, and available to pay current period liabilities.
>
> Expenditures for valid obligations when the department incurs the related liability and it is measurable, with the exception of the cost of employees' annual and sick leave. State accounting policy requires the department to record the cost of employees' annual leave and sick leave when used or paid.

The department uses accrual basis accounting for its Proprietary (Enterprise and Internal Service) and Fiduciary (Agency) fund categories. Under the accrual basis, as defined by state accounting policy, the department records revenues in the accounting period when realizable, measurable, and earned, and records expenses in the period incurred when measurable.

Expenditures and expenses may include: entire budgeted service contracts, even though the department receives the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

Notes to the Financial Schedules

Basis of Presentation

The financial schedule format is in accordance with the policy of the Legislative Audit Committee. The financial schedules are prepared from the transactions posted to the state's accounting system without adjustment.

Department accounts are organized in funds according to state law applicable at the time transactions were recorded. The department uses the following funds.

Governmental Fund Category

General Fund - to account for all financial resources except those required to be accounted for in another fund. The majority of the department's activity is recorded in this fund.

State Special Revenue Fund - to account for proceeds of specific revenue sources that are legally restricted to expenditures for specific purposes. The department has several State Special Revenue Funds that account for activities including supervision fees, canteen, inmate welfare, restitution, income and interest from state lands, and third party contributions for juvenile placement.

Federal Special Revenue Fund - to account for federal funds received by the department, including funds for Violent Offender Incarceration and Truth in Sentencing (VOITIS), substance abuse treatment, and various education programs.

Proprietary Fund Category

Enterprise Fund - to account for operations (a) financed and operated in a manner similar to private business enterprises, where the Legislature intends that the department finance or recover costs primarily through user charges; or (b) where the Legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes. Department Enterprise Funds include the Montana State Prison ranch and prison industries training programs.

Internal Service Fund - to account for providing goods or services to other agencies or departments on a cost-reimbursement basis.

Department Internal Service Funds include the Montana State Prison Industries Training and cook/chill Programs.

Fiduciary Fund Category

Agency Fund - to account for assets held by the state in a trustee capacity or as an agent for individuals, private organizations, other governments or other funds. Department Fiduciary Funds include moneys belonging to inmates of facilities and restitution for victims. The victim's restitution program went into effect on October 1, 2003.

2. General Fund Balance

The negative fund balance in the General Fund does not indicate overspent appropriation authority. The department has authority to pay obligations from the statewide General Fund within its appropriation limits. The department expends cash or other assets from the statewide fund when it pays General Fund obligations. The department's outstanding liabilities exceed the assets the agency has placed in the fund, resulting in negative ending General Fund balances for each of the fiscal years ended June 30, 2005 and June 30, 2006.

3. Direct Entries to Fund Balance

Direct entries to fund balance in the General, State Special Revenue, and Federal Special Revenue Fund types include entries generated by the state's accounting system to reflect the flow of resources within individual funds shared by separate agencies.

Department Response

DEPARTMENT OF CORRECTIONS

BRIAN SCHWEITZER, GOVERNOR

1539 11TH AVENUE

STATE OF MONTANA

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October 10, 2006

RECEIVED
OCT 11 2006
LEGISLATIVE AUDIT DIV.

Mr. Scott A. Seacat
Legislative Auditor
Legislative Audit Division
Room 135, State Capitol
PO Box 201705
Helena, MT 59620-1705

Re: Response to Legislative Audit Recommendations

Dear Mr. Seacat:

Thank you for the opportunity to respond to the financial-compliance audit report for the Department of Corrections. We have reviewed the recommendations contained in the report and our responses are as follows:

RECOMMENDATION #1:

We recommend the department develop a control structure, with an emphasis on training and communications, to help prevent or detect and correct financial and compliance issues.

Response:
Concur. The director will meet with the department management team and define specific criteria and expectations regarding the development of enhanced communication for all areas of the agency.

RECOMMENDATION #2:

We recommend the department record revenues and expenditures as required by state law and accounting policy.

Response:
Concur. Revenues and expenditures will be recorded as required by state law and accounting policy.

RECOMMENDATION #3:

We recommend the department establish policies and procedures, increase communication, and train staff to provide for consistent and efficient transaction processing.

Response:
Concur.

All federal grant activity will be recorded in accordance with GAAP with a monthly review completed by the Accounting Bureau chief.

Financial activity relating to the restitution account and the SABHRS receivable module has been corrected. All expenditure and revenue activity is recorded in the financial module of SABHRS.

All of Montana State Prison canteen financial information has been transferred from program 3 to program 4.

RECOMMENDATION #4:
We recommend the department implement controls to prevent and detect and correct accounting errors on a timely basis.

Response:
Concur. See individual responses below.

MCE certified work program: The department will define a policy to address the issues surrounding this recommendation. Federal regulations allow for the chief state correctional officer (director) to set regulations regarding room and board deductions for federally certified programs. The room and board collected from the workers in this program is used to offset the cost of offender programming provided by MCE.

Indirect costs to cannery operation: A letter will be sent to the food bank cannery regarding the indirect costs to the operation for fiscal year 2007.

Track customer orders and shipments: Staff and inmate clerks have been notified of the missing tickets and have been trained on the proper procedures.

Receivable balances: Balances will be reviewed monthly by an assigned accountant.

Pharmacy/medical bill review: Medical staff will work with provider to find a method of cross checking receivable reports with the invoices.

Industry training program: Fiscal year 2007 entries will be made to reflect prepaid expenses.

Payroll review: The review process is ineffective and has been discontinued.

Inmate payroll: The department will contact the regional prison and request appropriate submission of inmate payroll to enable timely reimbursement from the inmate welfare account.

Federal grant accounting: Federal grant accounting will be recorded in accordance with GAAP with appropriate cash draws to cover expenditures.

RECOMMENDATION #5:

We recommend the department ensure Montana Correctional Enterprises livestock assets are recorded in accordance with state policy.

Response:
Do not concur. According to the Department of Administration, all livestock assets have been recorded in accordance with state policy.

RECOMMENDATION #6:

We recommend the department implement adequate controls over contract administration.

Response:
Concur. The LAD recognized improvement in the area of contracts and the department will continue monitoring and notification efforts to ensure proper controls regarding state law references and contract compliance.

RECOMMENDATION #7:

We recommend the department:

A. Enforce the terms of the contract or seek reimbursement from the contractor for $25,000 paid under its transportation study contract.
B. Implement controls to ensure documentation required by contracts is received before approving contract payment.

Response:
Concur. The department has requested additional information from the contractor. If information is not provided, a request for repayment will be made.

RECOMMENDATION #8:

We recommend the department ensure it employees are enrolled in the proper retirement systems in accordance with state law.

Response:
Concur. The three instances listed have been corrected and human resources staff has modified the hire letter to include an internal check system to assure that an employee is placed in the correct system. Payroll will double check each employee's retirement placement whenever a transfer of position occurs.

RECOMMENDATION #9:

We recommend the department comply with state law regarding internal service funds, fees, charges and working capital.

Response:

Concur. We will work with the legislature to obtain an approved working capital balance in lieu of an approved rate.

Previous audit findings (Nov. 2002, Recommendation # 4) states "We recommend the department's cook/chill facility rates include a depreciation factor to ensure fees are commensurate with costs, as required by state law." However, now that depreciation is included in the rate calculation to comply with that audit recommendation, the working capital is increasing, and will continue to until the time that the equipment replacement takes place. This audit recommendation states the working capital balance exceeds the 60-day statutory limit. The food factory rate must include depreciation if there is to be adequate funding for replacement equipment. As equipment is replaced, the working capital will decrease.

RECOMMENDATION #10:

We recommend the department update, communicate, and distribute current policies to ensure compliance with its internal policies.

Response:
Concur. The department has revised the policy management system and is in the process of updating all department policies. Approximately 60 percent of policies have been updated and the remainder is on schedule for review. An Intranet-based employee policy access system has been developed and will be implemented by Dec. 31, 2006. Policies

that relate to department employee housing will be updated at the agency level and will address the rent issues.

RECOMMENDATION# 11:

We recommend the department continue implementing controls to ensure probation and parole officers and correctional officers receive training required by state law and department policy.

Response:
Concur. The Staff Development and Training Bureau, working with the Information Technology Bureau and state SABHRS staff has migrated department stand-alone training records database to the SABHRS "Training Records" module. This transition will provide the department with a stable records training platform and will include access by supervisors to employee training records. Training records consistency and availability will be enhanced by this change to the SABHRS module. Section 46-23-1003, MCA is also being reviewed for applicability. Department training policy is being reviewed to place responsibility for assuring department employees meet annual training requirements on direct supervisors and to a lesser degree the employees themselves.

RECOMMENDATION #12:

We recommend the department work with the legislature to appoint a member of the House of Representatives to the council as required by section 46-23-115, MCA.

Response:
Concur. The department will find a House member for appointment to the interstate compact council.

We appreciate the legislative staff time devoted to this audit. They were professionals throughout the process and their willingness to assist with any issue was exceptional. We look forward to working with your office in the future.

Sincerely,

Mike Ferriter

Mike Ferriter
Director